



Signed: May 18, 2006

Leslie Tchaikovsky

LESLIE TCHAIKOVSKY
U.S. Bankruptcy Judge

UNITED STATES BANKRUPTCY COURT
NORTHERN DISTRICT OF CALIFORNIA

In re
JOHN PAK,

No. 05-49326 TD
Chapter 7

Debtor.

MEMORANDUM OF DECISION

Sara L. Kistler, Acting United States Trustee, (the "UST") moves to dismiss the above-captioned case as an abuse of the Bankruptcy Code pursuant to section 707(b)(3).¹ For the reasons stated below, the motion will be GRANTED.

BACKGROUND

John Pak (the "Debtor"), an individual whose debts are primarily consumer debts, filed a voluntary petition seeking relief under chapter 7 of the Bankruptcy Code on October 31, 2005. Because this case was commenced after October 16, 2005, it is subject to the amendments to the Bankruptcy Code made by the Bankruptcy Abuse and

¹All statutory references are to Title 11 of the United States Code (the "Bankruptcy Code") unless otherwise specified.

1 Consumer Protection Act of 2005 ("BAPCPA"). As amended by BAPCPA,
2 section 707(b)(1) provides that a chapter 7 case filed by an
3 individual debtor whose debts are primarily consumer shall be
4 dismissed if the Court determines that it constitutes an abuse of the
5 Bankruptcy Code.²

6 The test for determining whether a debtor's case constitutes an
7 abuse pursuant to section 707(b)(1) varies depending on whether the
8 debtor's "current monthly income": (1) exceeds the applicable state
9 median or (2) is equal to or less than it. The case of a debtor
10 whose "current monthly income" exceeds the applicable state median is
11 subjected to a "means test." The "means test" consists of a
12 statutory formula for determining whether the debtor's income in
13 excess of his expenses is sufficient to permit him to pay a specified
14 amount or percentage of his nonpriority unsecured debts during a five
15 year period. If so, the statute creates a rebuttable presumption
16 that his case is abusive. See 11 U.S.C. § 707(b)(2)(A). This
17 presumption may be rebutted by evidence of "special circumstances."
18 See 11 U.S.C. § 707(b)(2)(B).

19 "Current monthly income" is defined as "the debtor's average
20 monthly income for the six calendar months prior to the filing of the
21 bankruptcy case." See 11 U.S.C. § 101(10A). Because the Debtor was
22 unemployed for most of the six calendar months preceding the filing
23 of his bankruptcy petition, the Debtor's "current monthly income"
24

25 ²Formerly, section 707(b) provided for dismissal only if the
26 case constituted a "substantial abuse." Moreover, there was a
statutory presumption in favor of granting the debtor relief. 11
U.S.C. § 707(b) (2002).

1 does not exceed the California median income and thus he is not
2 subject to the "means test." As section 707(b)(7) expressly
3 provides, his case cannot be dismissed based on the standard set
4 forth in section 707(b)(2).

5 This does not mean that his case may not be dismissed as an
6 abuse. The test for determining whether the case of an individual
7 chapter 7 debtor whose "current monthly income" is equal to or less
8 than the applicable state median is set forth in section 707(b)(3).
9 Section 707(b)(3) provides that a case may be dismissed as an abuse
10 based on: (1) bad faith or (2) "the totality of the circumstances ...
11 of the debtor's financial situation...." 11 U.S.C. § 707(b)(3).
12 There is no presumption of abuse under section 707(b)(3). The UST
13 brings her motion to dismiss this case under section 707(b)(3).

14 The UST does not contend that the Debtor has acted in bad faith
15 by filing his bankruptcy petition. Rather, she contends that "the
16 totality of the circumstances...of the [D]ebtor's financial
17 situation" make this case abusive. The Debtor is now employed,
18 earning slightly over \$100,000 a year. He is single, with no
19 dependents.

20 The Debtor opposes the motion on two grounds. First, he
21 contends that his ability to pay his debts is not part of the
22 "totality of the circumstances" test. Second, he argues that, even
23 if the Court may consider his ability to pay his debts in this
24 context, the totality of the circumstances of his financial situation
25 do not make his case abusive. The Court finds neither of these
26 arguments persuasive.

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ANALYSIS

A. CAN DEBTOR'S ABILITY TO PAY BE CONSIDERED UNDER SECTION 707(B)(3)?

At first blush, the Debtor's contention appears frivolous: i.e., that a debtor's ability to pay his nonpriority unsecured debts may not be considered as part of "the totality of the circumstances...of the debtor's financial situation." What could be more central to the debtor's financial situation than his income and expenses? However, a similar argument, albeit in a slightly different context, is made in a recent law review article authored by respected academics. See Marianne B. Culhane and Michaela M. White, Catching Can-Pay Debtors: Is the Means Test the Only Way?, 13 Am. Bankr. Inst. L. Rev. 665, 678-80 (2005)(the "Culhane-White Article").

The Culhane-White Article was written as a rebuttal to another recent law review article, authored by a Chicago bankruptcy judge, also highly respected for his expertise on BAPCPA. See Eugene Wedoff, Means Testing in the New 707(b), 79 Am. Bankr. L.J. 231 (2005) (the "Wedoff Article"). As noted in the Culhane-White Article, the Wedoff Article states that:

Because the general abuse provisions of § 707(b)(3) expressly apply when the means test has been rebutted, "passing" the means test does not preclude a discretionary finding of abuse by the court....If a debtor's overall financial circumstances would easily allow the debtor to repay debts...the court may find abuse.

1 Wedoff Article, at 236, n.8. Thus, Judge Wedoff posits that an
2 above-median debtor's case may be dismissed based on his ability to
3 pay under either section 707(b)(2) or (3).³

4 The Culhane-White Article disagrees with Judge Wedoff's
5 statement. It characterizes his view as a judicial attempt to "fix"
6 an imperfect statute. It opines that the plain language of the
7 statute and canons of statutory construction compel a different
8 conclusion. Culhane-White Article at 677.⁴

9 The rationale of the Culhane-White Article is as follows:
10 Section 707(b)(2) represents an attempt to remedy two pre-BAPCPA
11 problems, as perceived by Congress. First, section 707(b)(2)
12 establishes definitely that ability to pay, standing alone, is a
13 sufficient ground for dismissal as an abuse. Some courts had
14 previously taken a contrary view.⁵ Second, section 707(b)(2)
15 establishes a "bright line" test for a debtor's "ability to pay."
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17 ³Necessarily, the Court presumes, he would also conclude that
18 a below-median debtor's case could be dismissed based on his
19 ability to pay under section 707(b)(3), although not under section
20 707(b)(2).

21 ⁴As noted above, the issue addressed by these two articles
22 differs somewhat from the issue presented here. These articles
23 address whether a debtor whose "current monthly income" is above
24 the median but who passes the "means test" may have his case
dismissed based on his ability to pay under section 707(b)(3)(B).
The issue presented here is whether a debtor whose "current monthly
income is below the median (and thus is not subject to the "means
test") may have his case dismissed pursuant to section
707(b)(3)(B).

25 ⁵This does not represent a change in the law in the Ninth
26 Circuit. See In re Kelly, 841 F.2d 908, 913-15 (9th Cir.
1988)(ability to pay, standing alone, is sufficient basis for
section 707(b) dismissal).

1 One of the problems perceived by Congress in this context was the
2 lack of uniformity of bankruptcy courts' decisions on this issue.
3 Culhane-White Article at 678. According to the Culhane-White
4 Article, part of this "bright line" test is the establishment of the
5 median income as the dividing line for debtors whose ability to pay
6 may serve as the basis for dismissal. Culhane-White Article at 679.

7 According to the Culhane-White Article, "[t]o say that judges
8 are free under section 707(b)(3) to substitute their own can-pay
9 standards for Congress' means test would render the means test
10 superfluous." It would also go against the canons of statutory
11 construction, requiring statutes to be interpreted so as to be
12 consistent with each other and to give meaning to all parts. Id.
13 at 680.

14 The Debtor does not cite the Culhane-White Article. However,
15 he argues along similar lines. He notes that the "means test" was
16 established by Congress to eliminate the lack of uniformity in
17 judicial decisions on motions to dismiss under section 707(b). By
18 providing that the "means test" applies only to debtors whose
19 "current monthly income" exceeds the median, according to the Debtor,
20 Congress created a "safe harbor" for all other debtors.⁶ Any other
21 view would reintroduce the very judicial discretion that BAPCPA
22 sought to eliminate. The Debtor also quotes various statements by
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24 ⁶The "safe harbor" language appears to come from a statement
25 made by Senator Hatch. See 151 Cong. Rec. S1787 (February 28,
26 2005) ("[a]fter all these exemptions are applied, including the *safe*
harbor, it is estimated that 90 percent of debtor will not be
affected by the changes in the repayment provisions of this bill.
[Emphasis added]").

1 members of Congress, predicting that BAPCPA will have no effect on
2 debtors whose income is not above the median.

3 The Debtor recognizes that, but for the timing of his
4 unemployment and the statutory definition of "current monthly
5 income," he would fall into the category of debtors that Congress
6 wished to subject to the "means test." However, he notes that this
7 potentiality was "absolutely predictable to legislators." If
8 Congress had wished to prevent such debtors from falling through the
9 statutory cracks, it could have provided an express provision
10 preventing them from doing so. Courts may not remedy what Congress
11 failed to do.

12 There do not appear to be any reported decisions on this issue
13 to date. The only recent decisions addressing discrepancies between
14 actual income and expenses and the new statutory definitions for
15 income and expenses have been decided in the context of chapter 13
16 cases. See In re Jass, 340 B.R. 411 (Bankr. D. Utah); In re
17 Hardacre, 338 B.R. 718 (Bankr. N.D. Tex. 2006); In re Barr, ____
18 B.R. ____ (Bankr. M.D.N.C)(2006 WL 1030242). Because these cases
19 construe different statutory provisions, the Court does not find them
20 helpful.

21 There is a general canon of statutory construction that a
22 specific statute covering the same subject matter as a general one
23 will prevail over the more general one. This canon offers some
24 substantial support for the view taken by the Culhane-White Article.
25 However, this rationale cannot be applied to the debtor whose current
26 monthly income is equal to or less than the median. For this debtor,

1 there is no specific statute--i.e., "means test"--for determining his
2 ability to pay. There is only the more general one: i.e., section
3 707(b)(3).

4 The Debtor's argument that Congress knew that there would be
5 debtors whose actual income, due to pre-filing unemployment, would
6 be greater than their statutorily defined "current monthly income"
7 and could have provided for them is easily countered. By enacting
8 section 707(b)(3), Congress did provide for them.

9 The Court also finds instructive section 707(b)(3)'s use of the
10 phrase "the totality of the circumstances." Prior to BAPCPA, courts
11 considered whether to dismiss a consumer case for "substantial abuse"
12 under section 707(b)(1) based on the "totality of the circumstances."
13 See In re Price, 353 F.3d 1135, 1139 (9th Cir. 2004). All courts
14 considered the debtor's ability to pay to be an important factor in
15 this context. It would be counterintuitive to construe this same
16 phrase, as used in BAPCPA, to exclude a consideration of the debtor's
17 ability to pay.

18 The Debtor relies heavily on Congress's stated intention, in
19 enacting BAPCPA, to severely limit judicial discretion with respect
20 to section 707(b) motions so as to establish more uniformity. He
21 argues that, by construing section 707(b)(3) as including a
22 consideration of the debtor's ability to repay, Congressional intent
23 is subverted and judicial discretion is reintroduced into the system.
24 He also cites statements from the Congressional Record, assuring the
25 public that the below-median-income debtor's right to obtain
26 bankruptcy relief will not be affected.

1 The Court is not persuaded by these arguments. First, while
2 BAPCPA did severely limit judicial discretion for above-median-income
3 debtors, judicial discretion has not been entirely eliminated. As
4 noted above, the presumption of abuse may be rebutted by evidence of
5 "special circumstances." As to equal to or below-median-income
6 debtors, clearly, judicial discretion will have to be applied to
7 consider the "totality of the circumstances" whether or not those
8 circumstances include consideration of a debtor's ability to pay.
9 Finally, a debtor earning over \$100,000 a year cannot fairly complain
10 of being misled by Congressional statements that low income debtors'
11 rights to bankruptcy relief will not be affected by BAPCPA.

12 For all of these reasons, the Court concludes that the Debtor's
13 actual ability to repay his nonpriority unsecured debts may be
14 considered as part of the totality of circumstances of his financial
15 situation pursuant to section 707(b)(3).

16 **B. DOES DEBTOR'S CASE CONSTITUTE AN ABUSE UNDER "TOTALITY OF**
17 **CIRCUMSTANCES" TEST?**

18 As noted above, the Debtor's fallback argument is that, even if
19 his actual ability to repay his debts is considered, the totality of
20 the circumstances of his financial situation do not make his case an
21 abuse under section 707(b)(3). The UST disagrees. In support of her
22 motion, the UST cites In re Price, 353 F.3d 1135 (9th Cir. 2004), a
23 case decided prior to the enactment of BAPCPA. In Price, the Ninth
24 Circuit enumerated six factors to be considered in determining
25 whether to dismiss a consumer debtor's chapter 7 case as a
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1 "substantial abuse" pursuant to the former version of section 707(b)
2 as follows:

- 3 1) whether the debtor has a likelihood of
4 sufficient future income to fund a Chapter 11,
5 12, or 13 plan which would pay a substantial
6 portion of the unsecured claims;
- 7 2) whether the debtor's petition was filed as a
8 consequence of illness, disability,
9 unemployment, or some calamity;
- 10 3) whether the schedules suggest the debtor
11 obtained cash advancements and consumer goods on
12 credit exceeding his or her ability to repay
them;
- 13 4) whether the debtor's proposed family budget
14 is excessive or extravagant;
- 15 5) whether the debtor's statement of income and
16 expenses is misrepresentative of the debtor's
17 financial condition; and
- 18 6) whether the Debtor has engaged in eve-of-
19 bankruptcy purchases.

20 See Price, 353 F.3d at 1139. The UST contends that the majority of
21 these factors support dismissal of the Debtor's case as an abuse.
22 The Debtor disagrees.

23 The Court finds it unnecessary to resolve this dispute. Unlike
24 the statute addressed in Price, section 707(b)(3) contains two
25 prongs: (1) bad faith and (2) the totality of the circumstances of
26 the debtor's financial situation. Most of the Price factors listed
above pertain to the debtor's bad faith, not to his financial
situation. The only factor that pertains to his current financial
situation is his ability to pay his debts, e.g., through a chapter
13 plan. To analyze this factor, the Court must consider the
provisions of chapter 13, as amended by BAPCPA.

The principal issue in this context is which of the two incomes
of the Debtor to use in analyzing his ability to fund a chapter 13

1 plan: i.e., his "current monthly income" or his actual and projected
2 future income. Section 1325(b)(1) provides that, if the trustee or
3 an unsecured creditor objects to confirmation, the Court may not
4 confirm the plan unless, among other things, "the plan provides that
5 all of the debtor's projected disposable income to be received in the
6 applicable commitment period...will be applied to make payments to
7 unsecured creditors under the plan." 11 U.S.C. § 1325(b)(1).
8 Section 1325(b)(2) provides that "disposable income" means "current
9 monthly income received by the debtor...less amounts reasonably
10 necessary to be expended...[for the support of the debtor and the
11 debtor's dependents, charitable contributions, and necessary business
12 expenses] ." 11 U.S.C. § 1325(b)(2).

13 As discussed above, "current monthly income" looks back at the
14 debtor's income during the six calendar months preceding the
15 bankruptcy filing. 11 U.S.C. § 101(10A). The question is whether
16 the insertion of the word "projected" before the phrase "disposable
17 income" means that the Court should instead look forward, at the
18 debtor's actual and anticipated future income.

19 This question was recently addressed in a chapter 13 context in
20 In re Jass, 340 B.R. 411 (Bankr. D. Utah). In Jass, it was
21 contended that, after filing for bankruptcy, one of the joint debtors
22 had suffered a serious injury, thus increasing their expenses and
23 reducing their projected income. The debtors had an above-median
24 income. Thus, in calculating their projected disposable income,
25 section 1325(b)(3) required their expenses to be determined in
26 accordance with section 707(b)(2)(A) and (B). 11 U.S.C. §

1 1325(b)(3). Section 707(b)(2)(A) requires an above-median-income
2 debtor's expenses to be determined in accordance with guidelines
3 issued by the Internal Revenue Service in a form to be filed when the
4 case is commenced.⁷ The debtors contended that the use of the word
5 "projected" before the phrase "disposable income" indicated that
6 post-filing changes in circumstances should be considered. The Jass
7 court agreed. Id. at 414-16. It based its decision on the plain
8 language of the statute.⁸

9 A case more similar factually to the instant one is In re Barr,
10 ____ B.R. ____ (2006 WL 1030242), another chapter 13 case involving an
11 above-median-income debtor. In Barr, the debtor's financial
12 situation had improved since the six months preceding the bankruptcy
13 filing. The debtor's "current monthly income" showed a negative cash
14 flow whereas her actual disposable income was substantial. The
15 debtor did not want her post-filing change in circumstances to be
16 considered in the confirmation process. The Barr court concluded
17 that it should not be. However, it did not base its decision on a
18 construction of the phrase "projected disposable income."

19 In Barr, it appears, the only objection to confirmation made by
20 the chapter 13 trustee was based on lack of good faith. See 11
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23 ⁷Based on the calculations required by the "means test," the
24 Jass debtors could afford to pay \$3,625.63 to unsecured creditors.
In their plan, they proposed to pay only \$790.

25 ⁸Arguably, the debtors could have filed an amended "means
26 test" form to claim the additional expenses as "special
circumstances" pursuant to section 707(b)(2)(B). However, the
definition of "current monthly income" does not include any
category into which a post-filing reduction in income would fit.

1 U.S.C. § 1325(a)(3). The Barr court examined the evolution of
2 confirmation requirements and concluded that a debtor's ability to
3 pay could not be considered in determining good faith under section
4 1325(a)(3). Barr, at *1-*3. Thus, while the Barr court's decision
5 on the issue presented appears sound, it does not call into question
6 the correctness of the decision in Jass.

7 The Court agrees with the Jass court that the actual and
8 anticipated future income must be considered, rather than simply his
9 "current monthly income," in determining the debtor's "projected
10 disposable income" for purposes of confirming a chapter 13 plan.
11 Thus, this is also the correct income figure to use in deciding
12 whether to grant or deny a motion to dismiss a chapter 7 case under
13 section 707(b)(3)(B). The Debtor's actual monthly income at present
14 is \$5,530.20.

15 How the Debtor's reasonably necessary expenses should be
16 determined is not at issue. See 11 U.S.C. § 1325(b)(3). Section
17 1325(b)(3) provides that, if the debtor's "current monthly income"
18 is above the median, these expenses must be determined in accordance
19 with the section 707(b)(2)(A) and (B). However, the Debtor's
20 "current monthly income" is not above the median. Therefore, his
21 actual expenses provide the starting point, subject to reduction to
22 the extent the Court finds that they are not reasonably necessary.

23 The Debtor claims actual monthly expenses of \$3,718.00. This
24 leaves a projected disposable income of \$1,117.20. The UST argues
25 that some of the Debtor's expenses are excessive. Moreover, she
26 notes that, even without eliminating any of his claimed expenses, his

1 projected disposable income will allow him to make plan payments of
2 \$33,497.28 over a 36 month period.⁹

3 Because the Debtor has substantial unsecured debt, including
4 substantial nonpriority debt to the Internal Revenue Service, these
5 payments will only amount to 19 percent of his unsecured debts.
6 Thus, the final issue presented is whether a chapter 7 case is
7 abusive if a debtor could pay only a 19 percent dividend to his
8 creditors through a chapter 13 plan. Pre-BAPCPA, the Court generally
9 used a 33-1/3 percent "rule of thumb" in determining motions to
10 dismiss for "substantial abuse" under section 707(b). Three
11 considerations persuade the Court to grant the motion notwithstanding
12 the relatively low percentage payment that the Debtor is capable of
13 making to his creditors through a 36-month chapter 13 plan.

14 The first consideration is that, by removing the word
15 "substantial" from the phrase "substantial abuse," Congress appears
16 to have expressed an intent that a more stringent standard be
17 applied. This inference is clearly in keeping with the numerous
18 statements by members of Congress concerning the purpose of the
19 consumer amendments in BAPCPA. The second consideration is that,
20 while 19 percent is a relatively small percentage payment, \$33,497.28
21 is a relatively large amount. Finally, without making line-by-line
22 rulings, the Court agrees with the UST that some of the Debtor's
23 claimed expenses are excessive: e.g., \$150.00 per month for telephone
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25 ⁹Under BAPCPA, a debtor's "applicable commitment period" is
26 only 36 months if his "current monthly income" does not exceed the
median. 11 U.S.C. § 1325(b)(4)(A). In this context, "current
monthly income" is not modified by the word "projected."

1 services, \$850 per month to maintain two cars, and \$125.00 for
2 recreational activities. Based on all of these considerations, the
3 Court concludes that the Debtor's chapter 7 case constitutes an abuse
4 and should be dismissed or converted to chapter 13.

5 **CONCLUSION**

6 In summary, the Court concludes that, in determining whether to
7 dismiss the case of a debtor whose "current monthly income" does not
8 exceed the median under the "totality of the circumstances" test, the
9 Court should consider whether the debtor has the ability to pay a
10 significant portion of his unsecured claims through a hypothetical
11 chapter 13 plan. Second, in connection with this hypothetical
12 chapter 13 plan, the Debtor's "projected disposable income" should
13 take into account any post-filing change in circumstances, such as
14 increased or decreased income. Based on these legal conclusions, the
15 Court finds that the amount that the Debtor could pay approximately
16 19 percent of the claims of his nonpriority unsecured creditors over
17 36 months. Under the circumstances of this case, this makes his
18 chapter 7 case abusive under section 707(b)(3)(B).

19 The UST's motion is hereby GRANTED with a 14 day stay to give
20 the Debtor an opportunity to request conversion to chapter 13. The
21 UST is directed to submit an order consistent with the conclusions
22 of this Memorandum.

23 **END OF DOCUMENT**

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